FILE COPY

FILED
MAR 26 1937
CHARLES ELMORE CROPLEY
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1936

No. 667

ANNISTON MANUFACTURING COMPANY,
a Corporation,
Petitioner,

v.

HARWELL G. DAVIS, Collector of Internal Revenue,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF AMICUS CURIAE

RICHARD B. BARKER,
Southern Building,
Washington, D. C.

Of Counsel;
IVINS, PHILLIPS, GRAVES & BARKER,
Washington, D. C.

INDEX

	PAGE
PETITION FOR LEAVE TO FILE BRIEF AMICUS CURIAE	vi
BRIEF AMICUS CURIAE	1
Subject Matter of Brief	1
I. The statutory restrictions of Section 902 are not based upon any principle which permits the return of property unconstitutionally taken except in cases where such return would enrich the taxpayer unjustly	2
II. Even if Section 902 is based upon the doctrine of unjust enrichment it is impossible to apply that doctrine in this type of case..	7
III. Section 907 is either so indefinite in establishing a formula that it must be declared unconstitutional or is so arbitrary and capricious as to amount to a taking of property without due process of law	9
CONCLUSION	17

CASES CITED

Southern Pacific Co. v. Darnell-Taenzer Lumber Co., 245 U. S. 531	8

OTHER AUTHORITIES CITED

Congressional Library Catalogue Number		
HJ 141 A3 1898a	Adams, Henry Carter, *The Science of Finance*, New York, Henry Holt & Co., 1898	7

Congressional Library Catalogue Number		PAGE
HB 171 .5 A8	Atkins, Willard E., and Wubnig, Arthur, *Our Economic World*, New York, Harper & Bros., 1934	20, 25
HB 171 .5 A85	Ault, Otho C., and Eberling, Ernest J., *Principles and Problems of Economics*, New York, Longmans, Green & Co., 1936	27
HJ 141 B31	Bastable, C. F., *Public Finance*, (Third Edition), London, MacMillan & Co., Ltd., 1903	6
HB 171 C35	Carver, Thomas Nixon, *Principles of National Economy*, Boston, Ginn & Co., 1921	21, 24, 29
HB 171 .D4	Denslow, Van Buren, *Principles of the Economic Philosophy of Science, Government and Industry*, New York, Cassell & Co., Ltd., 1888	6, 23
HB 171 .5 A8	Ely, Richard T.; Adams, Thomas S.; Lorenz, Max O.; Young, Allyn A., *Outlines of Economics* (Fifth Revised Edition), New York, The MacMillan Co., 1930	19
HB 171 .F4 1922	Fetter, Frank A., *Modern Economic Problems*, Vol. II (Second Edition, Revised), New York, The Century Co., 1922	6, 23
HB 171 H3 1936	Harvard University, Graduate School of Business Administration, *Business Economics I*, Vol. I, February, 1936	25, 29
HB 171 H43 1928a	Hayes, Harry Gordon, *Our Economic System*, Vol. II, New York, Henry Holt & Co., 1929	19

Congressional Library Catalogue Number		PAGE
HB 171 H65	Hobson, J. A., *The Industrial System, An Enquiry into Earned and Unearned Income,* London, Longmans, Green & Co., 1909	19
HJ 2619 H6	Hobson, J. A., *Taxation in the New State,* London, Methuen & Co., 1919..	26
HB 171 H663	Hodson, H. V., *Economics of a Changing World,* New York, Harrison Smith and Robert Haas, Inc., 1933....	6, 20
HJ 141 H8 1928	Hunter, Harold, *Outlines of Public Finance,* New York, Harper & Bros., 1926	27
HB 171 K6	Knight, Bruce Winton, and Smith, Nelson Lee, *Economics,* Vol. II, New York, The Ronald Press Co., 1930....	20, 22
HJ 2305 M4	Means, David MacGregor, *The Methods of Taxation,* New York, Dodd, Mead & Co., 1909	25
HB 161 M6 1899	Mill, John Stuart, *Principles of Political Economy,* Vol. II (Revised), New York, The Colonial Press, 1899	21
HJ 2240 N3	National Tax Association, *Proceedings of 22d National Conference, 1929,* Published Columbia, South Carolina, 1930, by the National Tax Association	22, 25
HJ 2321 S44 1927	Seligman, E. R. A., *The Shifting and Incidence of Taxation,* Fifth Edition (Revised), New York, 1926	6, 8
HB 171 S56	Sidgwick, Henry, *The Principles of Political Economy,* (Third Edition), London, MacMillan & Co., Ltd., 1901	26

Congressional Library Catalogue Number		PAGE
HJ 2305 S65	Silverman, H. A., *Taxation, Its Incidence and Effects,* London, MacMillan & Co., Ltd., 1931	28
HB 171 T3 1930a	Taussig, F. W., *Principles of Economics,* Vol. II (Third Edition, Revised), New York, The MacMillan Co., 1930	24
HJ 2305 W4	Wells, David Ames, *The Theory and Practice of Taxation,* New York, D. Appleton & Co., 1900	22, 26
	Agricultural Adjustment, A Report of Administration of the Agricultural Adjustment Act May, 1933, to February, 1934, United States Department of Agriculture	11
	Agricultural Statistics, United States Department of Agriculture, 1936, Table 108	13
	American Tobacco Types, Uses and Markets, Charles E. Gage, Bureau of Agricultural Economics, Department of Agriculture, Circular No. 249, August, 1933	14
	Hearings before the Committee on Finance, United States Senate, 74th Congress, 2nd Session, on H. R. 12395	4
	Livestock, Meats and Wool—Market Statistics and Related Data, 1935. United States Department of Agriculture, June, 1936	16
	The Margin Between Farm Prices and Retail Prices on Ten Foods, Department of Agriculture	27
	Price Spreads Between the Farmer and the Consumer, by Richard O. Been, Jr., Agricultural Economist, and Frederick V. Waugh, Principal Agricultural Economist, United States Department of Agriculture, July, 1936	29

PAGE

The Processing Tax, United States Department of Agriculture, issued December, 1935 (G-41-Revised) 21

Senate Document No. 126, 74th Congress, 1st Session—"A Report on the Conditions and Problems of the Cotton Textile Industry Made by the Cabinet Committee appointed by Him [the President]", August 25, 1935..... 21

Senate Report No. 2156, 74th Congress, 2nd Session, on H. R. 12395..... 2, 10

IN THE

Supreme Court of the United States

OCTOBER TERM, 1936

No. 667

ANNISTON MANUFACTURING COMPANY,
a Corporation,
Petitioner,

v.

HARWELL G. DAVIS, Collector of Internal Revenue,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

PETITION FOR LEAVE TO FILE BRIEF AMICUS CURIAE

The undersigned respectfully petitions this Court for leave to file the subjoined brief as a friend of the Court.

RICHARD B. BARKER,
Southern Building,
Washington, D. C.

Of Counsel:
IVINS, PHILLIPS, GRAVES & BARKER,
Washington, D. C.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1936

No. 667

ANNISTON MANUFACTURING COMPANY,
a Corporation,
Petitioner,

v.

HARWELL G. DAVIS, Collector of Internal Revenue,
Respondent.

BRIEF AMICUS CURIAE

SUBJECT MATTER OF BRIEF

It is not intended that this brief be complete in itself or considered apart from that submitted by the petitioner. It will be confined to a limited phase of the question before the Court.

The restrictions upon the return of the money unconstitutionally taken from processors under the Agricultural Adjustment Act were justified before Congress upon the ground that the return of the money would permit the processors to be enriched at the expense of others; a doctrine

which has been termed "unjust enrichment".[1] In the lower courts the same theory or doctrine has been advanced.

It will be the purpose of this brief to show (1) that the law does not operate upon the basis of any such principle; that it does not prohibit the return of the taxpayer's property only in those cases where such a return would result in the enrichment of the taxpayer to an extent greater than would have been the case had there been no tax; it will further be shown (2) that if the law could be construed as based upon such a doctrine, it is impossible to determine or apply that doctrine in this type of case, and further to show (3) that the provisions of the statute are so indefinite in prescribing the formula to be followed that it is either unconstitutional for indefiniteness or is so arbitrary and capricious as to amount to the taking of property without due process of law.

I.

The Statutory Restrictions of Section 902 Are Not Based Upon Any Principle Which Permits the Return of Property Unconstitutionally Taken Except in Cases Where Such Return Would Enrich the Taxpayer Unjustly.

In other briefs filed in this Court it has been pointed out that taxpayers will not be "unjustly enriched" by the return to them of property which was unconstitutionally taken from them. With this principle we are thoroughly in accord. We believe, however, that there is a further situation arising out of the statute which should be called to the attention of the Court.

---

[1] Senate Report No. 2156, 74th Congress, 2nd Session, on H. R. 12395, pp. 32, 33.

Compare Title III of the Revenue Act of 1936 entitled "Tax on Unjust Enrichment".

Assuming, for the purpose of argument only, that one whose property has been taken contrary to law is not entitled to its return if the result would be to place him in a better condition than would have been the case had his property never been taken (that such recovery would constitute "unjust enrichment"), the restrictions imposed by the Revenue Act are not based upon any such doctrine.

Section 902 of the Revenue Act of 1936 provides that the taxpayers shall not be entitled to the return of their property or its equivalent,

> "unless the claimant establishes to the satisfaction of the Commissioner in accordance with regulations prescribed by him, with the approval of the Secretary, or to the satisfaction of the trial court, or the Board of Review in cases provided for under Section 906, as the case may be—
>
> (a) That he bore the burden of such amount and has not been relieved thereof nor reimbursed therefor nor shifted such burden, directly or indirectly, (1) through inclusion of such amount by the claimant, • • • in the price of any article with respect to which a tax was imposed under the provisions of such Act, • • • (2) through reduction of the price paid for any such commodity; or (3) in any manner whatsoever; • • •"

It is submitted that the statutory test bears little real relation to the question whether the return of the amount exacted from the processor would result in enriching him beyond the position in which he would have been had the tax never been exacted. Nevertheless the statute asserts that if the processor has increased the selling price of his goods by the amount of the tax, the recovery of the tax is not justifiable.

The statute overlooks entirely the damage and loss caused to taxpayers by the imposition of the tax. To illustrate: Assume that if no tax had been imposed, Processor A would have sold in a given year 10,000 articles at a selling price of $1.00 an article with a net profit of 25c per article. However, a tax was imposed on the raw materials which went into those articles equal to 5c per article and all other factors remained constant.[2] Processor A increases the selling price to $1.05 an article to which the public reacts unfavorably and buys only 8,000 such articles. The tax is declared unconstitutional and Processor A seeks to recover the $400 of taxes paid by him. This amount, added to his profit of 25c an article on 8,000 articles, would give him a total return of $2,400. His profit, if the tax had not been imposed, would have been $2,500. It is obvious that the recovery of the tax will not unjustly enrich A; that the necessary increase in the selling price has resulted in greater damage than the amount of the tax. That such a situation would result was brought out at the Congressional hearings, but the statute was not revised to remedy the situation.

The following is quoted from the record:[3]

> "SENATOR HASTINGS. Mr. Secretary, if the processor did only half as much business as he did in former years, after the tax was put on, and the margin of profit was the same, he might very well be making very much less for his concern, might he not?
>
> "MR. WALLACE. I think that would be an axiom, if he did only half as much business and had a small volume, he would be making less than half as much.

---

[2] Such a stability of other factors never really exists. In the example given, overhead costs would have to be distributed over 8,000 instead of 10,000 articles, necessarily reducing the net profit per article below 25c.

[3] Hearings before the Committee on Finance, United States Senate, 74th Congress, 2nd Session, on H. R. 12395, pp. 862-863.

"SENATOR HASTINGS. Then if your rules of determining the facts are based solely upon the difference in the margin, is that a correct rule in order to determine whether or not the processor is entitled to a return of his tax?

"MR. WALLACE. I do not think the Government would be responsible for the volume of the business done.

"SENATOR BAILEY. *The Government would not be responsible for the volume, but the increased taxes and the prices reduced the volume, and I think that should be a factor that should be taken into account.*

"MR. WALLACE. *I think you should take it into account.*

"SENATOR HASTINGS. *Is your amendment drawn so that it can be taken into account?*

"MR. WALLACE. *I do not think the amendments are drawn to take that particular point into account.*

"SENATOR KING. In determining the marginal differences which you have indicated on these charts, have you taken into account the factor, for instance, of imports, increased exports, or the change in the prices of foreign goods?

"MR. WALLACE. I do not see where that would enter into it. That has not been taken into account, Senator." (Italics supplied).

That the statute is not premised upon any principle of so-called "unjust enrichment" is further demonstrated by an examination of Section 907(e)(2). This section emphasizes the fact that the objective of the statute is to base the right of recovery on comparative selling prices and purchasing prices rather than upon any consideration of whether or not the recovery of the illegal tax would place the processor in better condition than would have been the case had no tax been imposed. The section provides that the Commissioner of Internal Revenue may rebut a prima facie case in favor of the taxpayer by showing:

> "• • • that the claimant modified existing contracts of sale, or adopted a new form of contract of sale, to reflect the initiation, termination, or change in amount of the processing tax, or at any such time changed the sale price of the article (including the effect of a change in size, package, discount terms, or any other merchandising practice) by substantially the amount of the tax or change therein, or at any time billed the tax as a separate item to any vendee, or indicated by any writing that the sale price included the amount of the tax, or contracted to refund any part of the sale price in the event of recovery of the tax or decision of its invalidity; • • •"

The principles which we have pointed out are not new. While economists differ in their terminology, they are in accord that there is a vast difference between (1) shifting the tax through raising selling prices or lowering purchasing prices, and (2) the economic effects of a tax on a taxpayer's business. The former is generally called "shifting the burden of a tax", while the latter is frequently called the "incidence", "pressure", "repercussion", or "economic effect" of a tax.[4]

It is therefore submitted that, assuming for the purposes of argument only that the doctrine of unjust enrichment might be a defense to the recovery of this tax, nevertheless Section 902 of the Revenue Act of 1936 is not a statutory declaration of this rule. Section 902 prevents recovery of the money unconstitutionally taken from the petitioner even though such recovery would still leave it poorer than it

---

[4] See: Seligman, E. R. A., *The Shifting and Incidence of Taxation*, Fifth Edition (Revised), New York, 1926, pp. 1 and 11; Bastable, C. F., *Public Finance*, Third Edition, London, 1903, pp. 360-361; Hodson, H. V., *Economics of a Changing World*, New York, 1933, pp. 222-224; Fetter, Frank A., *Modern Economic Principles*, Vol. II, New York, 1922; Denslow, Van Buren, *Principles of the Economic Philosophy of Science, Government and Industry*, New York, 1888.

would have been if the tax had never been imposed. The statute patently bears no relationship to any equitable doctrine of unjust enrichment and is therefore arbitrary, capricious and deprives the petitioner of its property without due process of law.

II.

Even If Section 902 Is Based Upon the Doctrine of Unjust Enrichment It Is Impossible to Apply That Doctrine in This Type of Case.

Assuming, but not admitting, that Section 902 is directed to the "pressure" or final "incidence" of the tax rather than its "shift" the processors are confronted with the impossibility of meeting the test of the statute. The petitioner has ably argued (brief, p. 34 to p. 40) the impossibility of proving whether or not a tax has been shifted by raising or lowering prices over what they would have been if the tax had never been imposed. It would seem patent that it is equally impossible to determine the "pressure" or final "incidence" of a tax. No other subject in the field of economics has given rise to such debate as the question of the shifting and economic effect or "incidence" of taxes—and still no definite conclusions have been reached. It has been said:[5]

> "As introductory to an analysis of the way in which taxes work, it is necessary to consider the shifting and incidence of taxes. There is perhaps no question respecting which so many conflicting views are entertained. Professor Seligman, whose ability to review bibliography and classify literature is unexcelled, shows in his chapter upon 'The History of the Doctrine of In-

[5] Adams, Henry Carter, *The Science of Finance*, New York, 1898, p. 388.

> cidence' that there are ten distinct groups of opinion entertained by writers upon this subject, and this of itself is adequate to suggest the care with which the student should enter upon its consideration."

As to all of these schools of thought, Professor Seligman says:[6]

> "Much—nay, by far the greater part—of the doctrine has come down to us in a systematic development from the original theories of the founders; but here and there excrescences are to be lopped off, gaps are to be filled."

With almost a dozen divergent theories confronting us, all of which require "loppings" and "fillings", the fundamental truth of Mr. Justice Holmes' statement in *Southern Pacific Co.* v. *Darnell-Taenzer Lumber Co.*, 245 U. S. 531, becomes obvious:

> "Behind the technical mode of statement is the consideration well emphasized by the Interstate Commerce Commission, of the endlessness and futility of the effort to follow every transaction to its ultimate result."

The writings of economists demonstrate the following fundamental proposition:

The subject of the "incidence" or "pressure" of a tax is a theoretical rather than a practical science; that economists only attempt to state tendencies as to the shifting of a tax and its "incidence" or "pressure" and as to such tendencies there is a vast divergence of opinion; and that the "incidence" or "pressure" of a tax cannot be made the subject of a mathematical computation as required by Section 902 of the statute.

Professor Seligman says:[7]

---

[6] *The Shifting and Incidence of Taxation* (5th Edition), p. 216.
[7] Ibid pp. 212-213.

"To the reader who understands the higher mathematics the hypothetical principles of the influence of tax on price can be illustrated with a degree of refined precision that is eminently satisfactory. But this advantage is occasionally secured at a heavy cost. While the intricate algebraic formulae may be worked out with perfect exactitude, the slightest flaw in a single symbol may invalidate the whole conclusion. Furthermore, the mathematical study of the pure theory often assumes a simplicity of condition which does not actually exist; it purposely neglects the all-important element of friction, and constructs hypotheses irrespective of their agreement with the facts of actual life. If, as sometimes happens, these hypothetical results are applied to the conditions of the market-place, the results are likely to be unreal."

It necessarily results that Section 902 of the Revenue Act of 1936 denies the taxpayer any remedy, for it is impossible to comply with its requirements. The statute is therefore arbitrary, capricious and unconstitutional.

III.

Section 907 Is Either So Indefinite in Establishing a Formula That It Must Be Declared Unconstitutional or Is So Arbitrary and Capricious as to Amount to a Taking of Property Without Due Process of Law.

If Section 902 establishes conditions precedent to the right to obtain a refund that are fundamentally defective, it would appear that any formula such as that provided by Section 907 would necessarily be tainted with the same fatal defects. These defects have been detailed in petitioner's brief, p. 40 to p. 51, wherein it is stated that Title VII

1. Creates an arbitrary and unreasonable presumption.

2. Unreasonably transfers the burden of proof to the processor.

It is submitted that fundamentally there is no difference in the degrees of unconstitutionality of Sections 902 and 907. It should be noted, therefore, that if Section 907 is declared unconstitutional, the Government should not be permitted to fall back on Section 902 and maintain that it is separable from Section 907. The inseparability of these provisions is further demonstrated by the legislative history of the adoption of Title VII of the Revenue Act of 1936. The Senate Finance Committee in its Report [8] points out that Section 902 is similar in principle to Section 21(d) of the Agricultural Adjustment Act, and goes on to say:

> "The imperative need of revising these provisions is apparent from a consideration of the administrative burden which confronts the Bureau of Internal Revenue, if claims for refund under the provisions of the Agricultural Adjustment Act must be passed on under Section 21(d) in its present form."

The Committee then goes on to state that Section 907 takes care of these as well as other difficulties. It is patent, therefore, that Congress never intended Section 902 to stand alone, and that if Section 907 is arbitrary, capricious and unconstitutional, the whole of Title VII must fall.

The petitioner in its brief has emphasized the fundamental defects involved in attempting to determine the incidence of a tax by comparing "spreads" in cost of raw materials and selling price of finished products between the period during which the tax is imposed and a period before and after the tax period. This fallacy has been emphasized, not only by economists generally, but has long been admitted by economists in the Department of Agriculture.

---

[8] Report No. 2156, 74th Congress, 2nd Session, pp. 32-34.

The most specific statement on the subject is in a report by the Agricultural Adjustment Administration, which stated:[9]

> "The question 'who pays the processing tax' cannot be answered by a mere examination of the change in producer, wholesale and retail prices and the final spread between them. It is true that commonly this question is answered in this partial way without taking into account such facts as the volume of supplies, the rate of consumption, the amounts paid by consumers, the total returns to producers, the benefit payments made to producers from the proceeds of the processing tax, the stimulus to general business activity through increased farm purchasing power, and the improvement in the credit structure of the country through enhancement of agricultural values."

The purpose of this amicus brief, however, is to emphasize the practical rather than the theoretical arbitrary nature of Section 907. That section is either so indefinite in establishing a formula that it must be declared unconstitutional,[10] or is so arbitrary and capricious as to amount to a taking of property without due process of law.

The fundamental basis of Section 907 is a comparison of cost price and sales value, and since these terms are defined by the statute, it is imperative to turn to those definitions. Section 907(b) (5) defines cost as follows:

> "The cost of commodity processed during *each month* shall be (a) the *actual cost* of the commodity processed *if the accounting procedure of the claimant is based thereon,* or (b) the product computed by multiplying the quantity of the commodity processed by the *current prices at the time of processing* for com-

[9] "A Report on the Administration of the Agricultural Adjustment Act, May 1933 to February 1934."

[10] See cases cited in petitioner's brief, p. 33.

modities of like quality and grade in the markets where the claimant customarily makes his purchases." (Italics supplied.)

It should be noted that the first determinative element is that the formula is based on monthly figures. Beyond that point, however, it is submitted that the formula for determining "cost" is unintelligible. It provides that the taxpayer should use *actual* cost figures if its accounting procedure is based on cost. Accounting procedure as set forth in the Revenue Act of 1936 and Regulations 96 issued pursuant thereto, involves such questions as accrual versus cash receipts and disbursements method of accounting; calendar year versus fiscal year method of accounting; long term contract versus completed contract basis of accounting, etc. The only place cost enters into a method of accounting is in the valuation of inventories, with respect to which the Income Tax sections of the Revenue Act provide that either "cost" or "cost or market whichever is lower" should be used. Patently, however, Section 907(b) (5) is not, or at least should not be concerned with the method of keeping inventories as a basis for determining shift in processing taxes.[11]

It is accordingly submitted that Section 907 is inherently defective in that the formula provided therein is so vague and uncertain that it is impossible for this Court to give it any definite meaning without invading the field of legislation.

But if we assume that the statute means that the cost figure is to be determined on the "a" or "b" basis dependent on whether the taxpayer reports its inventories on an "actual cost" basis as contrasted to an average cost, market, or some other basis, it is then submitted that the

---

[11] A tax cannot be shifted until the article is sold. See post p. 16 and discussion on the definition of selling value.

statute is clearly arbitrary and capricious. In the first place, there certainly can be no logical reason why shift in tax should be measured on the one hand by "actual cost," and on the other hand under Section 907(b) (5) (b), by a so-called "replacement cost". The arbitrary nature of such a provision can easily be demonstrated by the use of the Department of Agriculture's own figures.

Some processors of cotton tag each bale purchased and keep their production records in such shape that they know when any particular bale of cotton is processed. Other processors merely inventory their cotton on an average rather than an "actual" cost basis. The first processor, whom we will call A, bought a large supply of cotton in June of 1932, when the average spot price per pound of "7/8 middling" at ten combined markets was 4.99c per pound.[12] The second processor, whom we will call B, also bought a large supply of the same cotton at the same price. A, however, carefully tagged his bales, and so when he used that cotton along with other cotton purchases in October of 1933, he knew the "actual" cost to be 4.99c per pound. B, on the other hand, merely averaged the price of his cotton purchases, and although he used the cotton purchased in June of 1932 in October, 1933, his records merely showed the average cost of all his cotton purchases. Consequently, since B's records do not show "actual" cost of the cotton used in October, 1933, he is entitled to determine his cost by "multiplying the quantity of the commodity processed by the *current* prices at the time of processing." The average spot price of "7/8 middling" in October, 1933, at ten combined markets was 9.16c.

Thus A because he has kept more detailed records than B uses a cost figure of 4.99c per pound, whereas B uses a

---

[12] Agricultural Statistics, United States Department of Agriculture, 1936, p. 83, Table 108.

PRE TAX PERIOD (1932)

2.	3.	4.	5.	6.	7.	8.
ost per lb.	*Selling Price per lb.*	*Margin*	*Cost Basis Used*	*Average Cost per lb.*	*Tax per lb.*	*Comb Co*
8.3c	30c	21.7c	Actual Cost of 1931-1933 Fire-Cured Type 21	6.6c	2.14c	8.7
8.2c	30c	21.8c	Reproduction Cost of 1933-1935 Fire-Cured Type 21	9.43c	2.14c	11.5

cost figure of 9.16c per pound, or a difference in cost basis of 4.17c per pound. Since the processing tax on a pound of cotton was 4.2c per pound, it is obvious that, disregarding all other factors, B can show a lower spread between cost and selling value by almost the amount of the processing tax.

The arbitrary character of the statute is even more strikingly illustrated in the case of tobacco. In the case of snuff the tobacco is stored for a period of upwards of two years before it is used. A tags his hogsheads of tobacco, and must therefore use "actual" cost. B, on the other hand, merely averages his costs and therefore must use "reproduction" cost. Both A and B sell the same type of product—say a 10c package of snuff. They both buy their tobacco at the same auction sales in open competition with one another. The processing tax on snuff tobacco is 2.14c per pound, and it will be assumed that a pound of tobacco, farm weight, is required to make three packages of snuff.[13]

With these assumed facts before us, and using the statistics of the Agriculture Department,[14] let us apply the statutory formula prescribed by Section 907:[15]

TAX PERIOD 1933-1935

4.	5.	6.	7.	8.	9.	10.	11.	12.
Margin	*Cost Basis Used*	*Average Cost per lb.*	*Tax per lb.*	*Combined Cost*	*Selling Price per lb.*	*Margin*	*Difference in Margin Column 4-10*	*Tax Absorbed per Pound, i.e., Amount of Refund*
21.7c	Actual Cost of 1931-1933 Fire-Cured Type 21	6.6c	2.14c	8.74c	30c	21.26c	0.44c	0.44c
21.8c	Reproduction Cost of 1933-1935 Fire-Cured Type 21	9.43c	2.14c	11.57c	30c	18.43c	3.37c	2.14c

[13] Fire-cured tobacco is the principal tobacco used in the manufacture of snuff. American Tobacco Types, Uses and Markets, Charles E. Gage, Bureau of Agricultural Economics, Department of Agriculture Circular No. 249, Aug. 1933, p. 12.

[14] Agricultural Statistics, United States Department of Agriculture, 1936, p. 108, Table 147.

[15] The figures for the post-tax period (Sec. 907(c)) are not published as yet and are not used in the illustrative case.

Thus, if the formula prescribed by Section 907 is of sufficient clarity to be possible of application, it is apparent that processor B receives a refund almost 500% larger than A receives. This results not because they buy their tobacco at different prices or sell their products at different prices or any other differences in cost, merchandising overhead, taxes, etc., but merely because A kept more detailed accounting records than B so that A could ascertain his actual monthly cost of tobacco used whereas B had only an average cost figure of all tobacco contained in his warehouses.

It is submitted that the above practical application of the statute is sufficient to justify a decision of its unconstitutionality on the ground that it arbitrarily and capriciously deprives a taxpayer of his property without due process of law.

The "cost" is only one element in determining the "shift" of the tax. The Court's attention is directed to the statutory definition of "Gross sales value of articles". Section 907(b)(6) defines this provision as follows:

> "The gross sales value of articles shall mean (a) the total of the quantity of each article derived from the commodity processed by the claimant during each month multiplied by (b) the claimant's sale prices current at the time of processing for articles of similar grade and quality." [16]

The above definition of sales value discloses that the presumption established by the statute has no reasonable rela-

---

[16] It must be remembered that we are dealing with a statute that establishes a presumption as to whether or not the taxes imposed by the Agricultural Adjustment Act were shifted or absorbed by the taxpayer. It is therefore essential that the ultimate fact presumed must bear a reasonable relationship to the facts upon which it is based. (See brief of petitioner, p. 40 to p. 48.) It is not sufficient that the parties are entitled to rebut the presumption.

tionship to the facts on which it is based. We take it that it is elementary that a tax cannot be shifted unless and until the article on which the tax is placed is sold. Section 907(b)(6), however, does not deal with actual sales but with hypothetical sales value. In other words, in working out the presumption, the sales figure is based upon the fiction of what the article *would have sold for* if it had been sold during the month in which it was processed. The statute totally disregards actual facts and proceeds on the basis of fictional values, which in many, if not most, instances, are contrary to actual facts. It is submitted that this Court should take judicial notice of the fact that in this day and age of large scale production and distribution, most manufacturers have inventories of finished goods on hand from which they can make their sales for months in advance. Certainly, this Court should recognize that many businesses are seasonal in nature, e.g., the blanket industry, and a processor may spend months building up an inventory which he can sell during a short selling period. To say that for the purposes of determining shift in tax the sales figure should be based upon price for a certain month, when the actual sales figure may be dependent upon prices occurring many months later, taxes human credulity beyond all bounds of reason. Thus, for example, bacon and hams are cured from 30 to 90 days. A hog might have been processed in September, 1934, when the retail price of smoked picnics (ham) was 16c per pound. Assume a 60 day cure, and further assume that the picnic was sold immediately after the curing was finished, the actual sale price would have been 14c per pound.[17] The statutory presumption would be determined upon a sales figure of 16c, whereas the actual sales price was 14c, or an initial discrepancy of 2c a pound. Con-

[17] Livestock, Meats and Wool—Market Statistics and Related Data, 1935. United States Department of Agriculture, June, 1936, p. 132.

sidering the fact that the processing tax per pound imposed on the picnic was only 1.82c per pound,[18] it is patent that the statutory presumption bears no reasonable relationship to the actual facts and should be declared unconstitutional.

CONCLUSION

In support of the arguments made in this brief, an appendix containing extracts from the writings of numerous economists has been attached. The Court's attention is respectfully directed to the following classification of the appendix.

A. *The "Pressure," "Incidence" or "Economic Effects" of Taxes.*

The economists agree that the "pressure" or "incidence" of a tax has real economic effects on a taxpayer and, even assuming he is able to shift the burden of the tax, may leave him poorer than he would have been if the tax had never been imposed.

B. *Impossibility of determining "Pressure," "Incidence" or "Economic Effects" of Taxes.*

The economists agree that the determination of the "pressure" or "incidence" of a tax is an impossible task because so many related factors must be taken into consideration and that the comparison of cost price to sales value as between two different periods of time cannot serve as a reasonable basis for deter-

---

[18] T. D. 4518, and regulations issued pursuant thereto. Reported at 1935 CCH ¶ 1983-A-12.

mining the "pressure" or "incidence" of a tax or even the shift of the burden of the tax.

Respectfully submitted,

RICHARD B. BARKER,
Southern Building,
Washington, D. C.

Of Counsel:
IVINS, PHILLIPS, GRAVES & BARKER,
Washington, D. C.

APPENDIX A

The "Pressure," "Incidence" or "Economic Effects" of Taxes

1. Hayes, **Our Economic System**, Vol. II, pages 318-319.

"As was emphasized in the discussion of the prices of goods produced by concerns that have large fixed plants, **the imposition of a tax upon units of output will normally be borne by the owners of the industries in question.** Such concerns should increase the price of their products only by reducing the supply of them. But to reduce the supply would mean that the average cost of production would be increased, since the total overhead would be spent on a fewer number of units than had formerly been the case. Hence, under such conditions, a business concern might find that its net loss would be less by bearing the tax, than by shifting it to the consumers of the product."

2. Ely, **Outlines of Economics**, page 793.

"The word 'shifting' usually refers to the increase of price by which the original payer of the tax attempts to recoup himself. This increase of price is usually accompanied by collateral economic disturbances or dislocations—suggested by the phrase 'repercussion of taxes' which is frequently employed in this connection—that are quite as important as the mere change in price. For instance, an excise tax (per unit of product) upon a monopoly may raise the price by as much or even more than the tax itself. But the monopolist nevertheless feels the burden of the tax in reduced profits. **When we say that a tax is shifted, then, we do not imply that the original payer evades *all* the evil effects of the tax.**"

3. Hobson, **The Industrial System**, page 229.

"From this reasoning, if it be correct, there issue two conclusions. First, that a tax imposed in the first in-

stance upon an income which is a subsistence wage, or any minimum cost of production, tends to be moved on until it finds, in the course of its shifting, elements of 'surplus income' on which to settle. Second, that **no consumer, as consumer, can be considered to have any ability to bear a tax; taxes must ultimately be held to be paid out of such incomes as can bear them.**

"In any scientific analysis of incidence of taxes, we must trace the incidence to incomes derived from ownership of some factor of production, that is to say, **all taxes are ultimately borne by certain classes of producers.**"

4. Hodson, **Economics of a Changing World**, pages 222-224.

"In the short run, the ability of producers to lower their prices to the level of prime costs, that is to say until their fixed capital becomes not merely unremunerative compared with the return obtainable on investment elsewhere, but actually worthless, may mean that competition will force down the net price to a point at which volume of sales and the gross price to the buyer are approximately the same as before, but in the long run, as unremunerative capital gets squeezed out, a higher price and a lower volume of sales are to be expected. **In either case, the seller pays the greater part of the tax.**"

5. Atkins, **Our Economic World**, pages 371-372.

"**Moreover, a tax intended to assess householders** (owners of furniture, radios, refrigerators and automobiles) **may actually strike at the profits of the manufacturing companies.**"

6. Knight, **Economics**, Vol. II, pages 919-920.

"In a sense it is misleading to speak of the 'ultimate incidence' of taxes for, because of the interrelations already indicated between taxation on the one

hand and production, consumption, and distribution on the other, **all taxes must, in last analysis, bear most heavily upon those who own, at the time the full effects of the tax are felt, the relatively fixed agencies of production.**"

7. Carver, **Principles of National Economy**, page 630.

"The buyer of what one has to sell and the seller of what one has to buy will have something to say about it. Unless the tax affects the general conditions of the market in a way which favors the payer of it, he will not be able to sell at a higher or buy at a lower price—in other words, **he will not be able to shift the tax.**"

8. Mill, **Principles of Political Economy**, Vol. II, page 343.

"**Taxes on necessaries must thus have one of two effects. Either they lower the condition of the laboring classes; or they exact from the owners of capital, in addition to the amount due to the state on their own necessaries, the amount due on those consumed by the laborers.** In the last case, the tax on necessaries, like a tax on wages, is equivalent to a peculiar tax on profits; which is, like all other partial taxation, unjust, and is especially prejudicial to the increase of the national wealth."

APPENDIX B

Impossibility of Determining "Pressure," "Incidence" or "Economic Effects" of Taxes

1. Senate Document No. 126, page 24.

"**It is impossible to disentangle the effect of any individual element of cost upon selling price.**"

2. Department of Agriculture, **The Processing Tax**, page 8.

"**As a practical matter, it is impossible completely to separate the effects of the processing taxes from the**

effects of the adjustment programs on prices farmers receive or consumers pay for agricultural products. Nor is it possible completely to separate the effects of the adjustment programs from the effects of the drought, the devaluation of the dollar, expenditures for relief, and general business recovery on prices of agricultural products."

3. National Tax Association, **Proceedings of 22d National Conference, 1929.** From an article entitled "Consumption Excise Taxes as Relief for the Tax Burden on Farm Property", by S. M. Derrick, page 271.

"But as a matter of fact it is by no means certain that property and business taxes are shifted to the ultimate consumers. **The whole matter of the shifting and incidence of taxation is in a controversial stage.**"

4. Wells, **The Theory and Practice of Taxation,** page 569.

"No attempt ought to be made to construct or formulate an economically correct, equitable, and efficient system of taxation which does not give full consideration to the method or extent to which taxes diffuse themselves after their first incidence. On this subject, there is a great difference of opinion, which has occasioned, for more than a century, a vast and never ending discussion on the part of economic writers. **All of this discussion, however, has resulted in no generally accepted practical conclusions**; has been truthfully characterized by a leading French Economist (M. Parieu) as marked in no small part by the 'simplicity of ignorance', **and from a somewhat complete review (recently published) of the conflicting theories advanced by participants one rises with a feeling of weariness and disgust.**"

5. Knight, **Economics,** Vol. II, pages 919-920.

"Since, however, the current operation of every tax is affected by the past effects of this and of all other taxes as well as by the simultaneous operation of what-

ever other taxes co-exist in the revenue system, **it is an exceedingly complex matter to uncover the exact** *final resting place* **of any particular tax.**"

6. Fetter, **Modern Economic Problems**, Vol. II, pages 283-284.

"The lawmaker cannot tell exactly where the weight will fall. **The principles of value give some guidance in the inquiry, but the workings of the principle are difficult to follow.**"

7. Denslow, **Principles of the Economic Philosophy of Science, Government and Industry**, pages 462, 465, 467.

"It has never occurred to the writers on this subject, that if the ultimate incidence, or final deleterious effect, of a tax or burden can be defined, much more by parity of reason ought we to be able to define where the benefits of production, or of a new aid to production, stop. We ought to be able to point out the extreme outward person upon whom the beneficent effects of the invention of printing, the discovery of America, or of gold in California, rests. A tax, considered as a diminution of production, can hardly be measured until we can assign limits to the effects of aids to production. For peradventure, the tax itself may be an aid to production, and in that case it has no incidence, properly speaking, since its supposed 'blow' is converted into a caress.

* * * * * * *

"**There are those who feel confident to decide, amidst this congeries of mazy influences, radiating outward indefinitely through all the transactions of mankind, what the ultimate incidence of a tax may be. To me it seems as hopeless as to attempt to set bounds to the causative operations of a winter's snow or a summer's rain.**

* * * * * * *

"**The notion, that the incidence of taxes should be made certain, is like the kindred notion, that the law**

should be made simple. It demands an impossibility in finance.''

8. Carver, **Principles of National Economy**, page 630.

''One of the first lessons that the student of taxation learns is that the payer of a tax sometimes shifts the burden in whole or in part on to someone else, thus relieving himself, in part at least, of the burden. This can come about only in the process of buying and selling. **The person taxed, in other words, has no means of persuading anyone else, as a favor to himself, to assume the burden**; he can only charge a higher price for what he has to sell, or pay a lower price for what he buys, thus recouping himself for what he has paid in the form of a tax. **But this matter of raising the price of what one has to sell or depressing the price of what one has to buy is something which is not so easily done as said, as anyone can convince himself by trying it.''**

9. Taussig, **Principles of Economics**, pages 557-558.

''The very statement of this last case points to an important limitation on the pertinence of all such analysis. There is danger of making an intellectual plaything out of intricate reasoning on the play of demand, varying costs, taxes and the like. **Some economists have given no small share of attention to problems of this kind, forgetting that their reasoning is purely hypothetical and that there is little that corresponds to it in the concrete facts of life. All economic principles hold good only in the rough. Semi-mathematical reasoning, even pure mathematical reasoning,** not infrequently aids in bringing out with clearness the underlying principles; but it **can rarely be pushed with advantage into details.** It cannot be so pushed with reference to the incidence of taxes—neither as regards the modification of incidence due to increasing or diminishing returns, nor as regards the effect of taxes on monopolized articles.''

10. Atkins, **Our Economic World**, pages 371-372.

"It would be hard to determine, again, whether or not commodity taxes can be shifted wholly from the producer to the consumer. In a period of rising prices and quick sales (a 'seller's market'), the business enterprise may find it easy to pass along commodity taxes by charging higher prices. In a period of falling prices and slow sales (a 'buyer's market'), the business enterprise may be compelled to bear the costs of commodity taxes, finding itself unable to push up the price to discount the tax in full."

11. Harvard University, **Business Economics I.**, From the article by Richard S. Meriam, "Some Notes on Cotton Prices and the Processing Tax," Appendix B, page 15, February, 1936.

"The prices of some commodities, of which cotton is one, are affected by speculation, by speculative anticipation of eventual results. This factor cannot be ignored in forming an opinion of the incidence of the cotton processing tax."

12. Means, **The Methods of Taxation**, pages 237-238.

"It follows also that the intent of the legislature that particular persons shall pay the tax imposed by a general law constitutes no presumption that such persons will really carry the burden of the tax. That this is true in many cases, and to a great extent, is disputed by nobody; **but in what cases, and to what extent, even if discoverable by experts, is not generally understood."**

13. National Tax Association, **Proceedings of 22d National Conference, 1929**, page 271.

"A tax on business may or may not be shifted; depending upon the matter of monopoly, the conditions of the cost of production, the nature of the business, and other factors of varying importance. **Certainly, no definite conclusion can be reached that this position is valid."**

14. Wells, **The Theory and Practice of Taxation**, pages 570-571.

"It is essential at the outset to correct reasoning that the distinction between *taxation* and *spoliation* be kept clearly in view. That only is entitled to be called a tax law which levied uniformly upon all the subjects of taxation; which does not of itself exempt any part of the property of *the same* class which is selected to bear the primary burden of taxation, or by its imperfections to any extent permits such exemptions. **All levies or assessments made by the State on the persons, property, or business of its citizens that do not conform to such conditions are spoliations, concerning which nothing but irregularity can be predicated**; nothing positive concerning their diffusion can be asserted; and the most complete collection of experiences in respect to them cannot be properly dignified as 'a science'."

15. Hobson, **Taxation in the New State**, page 53.

"But enough has been said to indicate the subtly psychological factors which here help to determine the effect of a rise of price upon demand for different classes of commodities. **The incidence of a tax will vary with their subtle pressures**. We can never treat any tax upon commodities as obviously transferable to the 'consumer', even in the process of finding producers surpluses in which to settle. Some of it will generally pass, **but how much no one can predict**. Some of it will be thrown back on the various sets of producers or carriers or vendors."

16. Sidgwick, **The Principles of Political Economy**, page 570.

"**Indeed this process is often so complicated and obscure that it is a problem of considerable intricacy and difficulty to ascertain where the burden of a tax actually rests**; and it is not even a simple matter to state accurately the general principle for determining the incidence of a tax, supposing all the facts to be known."

17. Hunter, **Outlines of Public Finance**, pages 157-158.

"**It would be utterly impossible to trace the burden of every tax until the incidence were definitely determined.** In fact, it would be impossible to trace definitely, through all its ramifications of direct and indirect influences the shifting and effects of any tax burden, though it could be much more nearly done in some cases than in others."

18. Ault, **Principles and Problems of Economics**, page 588.

"**The shifting of some taxes is not so easily traced.** The Physiocrats held that only the extractive industries produced a surplus, *produit net*, and that consequently all taxes finally revert to the owner of natural resources; therefore, they advocated a single tax on land, the *impot unique*. Later it came to be held, particularly among business men and politicians, that any tax after a time became diffused among the citizens of the state so that each finally bore his just and equitable share of the tax burden. This is known as the diffusion theory of tax shifting.

"Were taxes shifted as evenly and universally as the diffusion theorists hold, justice in taxation would be a simple matter. Our legislators would need only to select a good revenue-yielding tax and stick to it. In time, according to the diffusion theory, the burden of taxation would be equitably distributed. But studies of the diffusion theory do not substantiate this claim. It is found that some taxes are shifted in various ways and in varying degrees, while other taxes are not shifted at all."

19. Department of Agriculture, **The Margin Between Farm Prices and Retail Prices on Ten Foods**, pages 10-11.

"There are two principal reasons for long-time changes in the spread between prices at the farm and in the city store. They are, first, changes in costs including wages, transportation rates, material costs and cost of other items, and second, changes in the efficiency

of processing, marketing, and distribution. In addition to changes in those factors there are doubtless changes in the profits of processors and distributors.

• • • • • • •

"The recent growth of chain store distribution, the increasing number of general food stores handling both groceries and meats, the reorganization of city market terminals, and many similar changes have doubtless affected efficiency to some extent.

"Also, there have been significant changes in the processing and packaging of the food products themselves which affect costs. Examples of such changes are the development of small packages, the slicing of meats and bread and the drop in bulk sales of many foods. Some of these changes make accurate comparisons of present prices with pre-war prices very difficult because the consumer is really buying a different food today and in many cases is paying for more processing and packaging."

20. Silverman, **Taxation, Its Incidence and Effects**, pp. 93, 114.

"Conversely, price movements may coincide with variations in the rate of taxation, yet be attributable in part to altogether different factors.

• • • • • • •

"**Similarly, one cannot measure the exact incidence of a tax on imported articles such as motor cars by comparing the prices at dates before and after the imposition of the duty.** All sorts of factors enter into the determination of motor car prices, many of them entirely independent of, and much more important than, changes in the scale of taxation. Following the re-imposition of the 'McKenna duties' the price of some foreign cars increased while those of others declined. Obviously, reasons other than taxation were largely responsible for the price movements. This argument goes to show the imprudence on relying on price statistics for a reliable

guide to incidence. In no other branch of applied economics must figures be used with greater caution.

* * * * * * *

"It was shown, first, that price movements following the imposition or increase of a tax do not necessarily indicate the extent to which it has been shifted."

21. Harvard University, **Business Economics I.** From the article by Richard S. Meriam, "Some Notes on Cotton Prices and the Processing Tax," Appendix B, page 15, February, 1936.

"**It may be said with confidence that the notion that a tax on a commodity always raises the price at once by an amount equal to the tax is not held by any modern economist.**"

22. Carver, **Principles of National Economy,** pages 631-632.

"**There is a more or less general opinion that the value of anything is determined directly by what it costs, and that as a tax adds to the cost it must therefore be added to the price. This overlooks the true relation of cost to value.** The cost of anything affects its value only when it puts a check upon production and limits the supply. Whenever an addition to the cost will cause a decrease in the supply or an increase in the demand, it will raise the value of the article in question. But this will not occur in every case. It is scarcely conceivable that a tax can increase the demand for the thing taxed. If it ever does so, the instances must be so rare that we can safely ignore them. This leaves us to the conclusion that a tax can raise the price of the thing taxed only when it occasions a diminution in the supply."

23. Department of Agriculture, **Price Spreads Between the Farmer and the Consumer,** page 12.

"The relation of margins to supply could be derived theoretically from the relation of margins to price through the supply-price function, after variation in the price level had been eliminated, **but supply-price functions themselves are sometimes vague and unreliable.**"